

# Consumers Price Index – 2020Q3

23 October 2020



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## Contact

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## Not a great place to start

- CPI rose 0.7% q/q in Q3 to see annual inflation moderate from 1.5% y/y to 1.4%. A stronger bounce had been expected following last quarter's lockdown-impacted fall (-0.5% q/q).
- The data has taken a backseat right here and now, partly due to noise; we won't know where the trend is settling until early next year at least. But given the RBNZ are more worried about downside risk than upside, the deceleration will be concerning.
- From today's weak starting point, the outlook is for softness in inflation over the medium term, and current low inflation now could serve to reinforce low inflation expectations. The case for more monetary stimulus remains clear for now, with an [FLP expected](#) to be deployed in November.

## Key points

CPI increased 0.7% q/q, weaker than market consensus (0.9%), our own forecast, and RBNZ expectations at the time of the August MPS (1.1% q/q). Annual inflation fell to 1.4% y/y, after falling from 2.5% to 1.5% last quarter.

Today's data were impacted by measurement issues, weight changes and volatility, as highlighted in our [CPI preview](#), making forecasting more difficult than usual and reducing the amount of signal that can be gleaned from today's data. We won't be able to get a sense of where the trend in inflation is settling until the new year, even if we remain COVID-free and further disruption is avoided. For now, though, core inflation appears to be drifting lower, to be by and large below the RBNZ's target midpoint.

The RBNZ is clearly more concerned about downside risk than upside at present – and the starting point matters. With annual inflation well below the 2% target range midpoint and the medium-term outlook suggesting disinflationary forces will mount, the RBNZ has its work cut out. A weak starting point for inflation has the potential to reinforce low inflation expectations, which are currently at dismal levels (see figure 4). And with the economic recovery set to stagnate, job losses expected to rise and a more challenging time ahead, inflation is set to be too low and unemployment too high. The case for more stimulus remains clear for now.

We expect that today's data will add to broader concerns for the RBNZ, given ever-present downside risks. It's more at the margin than usual, of course, reflecting potential noise in the data, but with the RBNZ hyper-vigilant to downside risks, today's print will not go unnoticed – it's simply not a great place to start.

Over time, strategy around policy setting for the RBNZ is expected to become more nuanced, but we are not quite there yet. We see the RBNZ implementing an FLP in November, followed by a negative OCR next year. How much further stimulus is ultimately required will depend on the effectiveness of these policies and other economic developments, but for now we think the RBNZ will remain firmly of the view that more needs to be done.

Turning to the details:

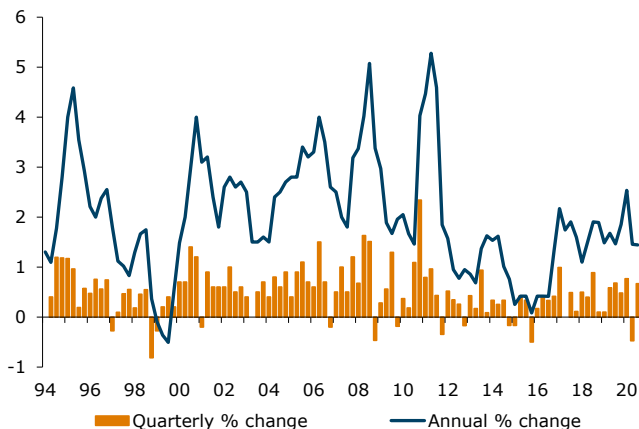
- Both tradable and non-tradable prices rose 0.6% q/q. This saw annual tradable inflation increase from -0.6% y/y to -0.1%, still very weak. Non-tradable inflation now sits at 2.6% y/y, after drifting down from 3.1% last quarter and 3.4% in Q1.

## Data summary

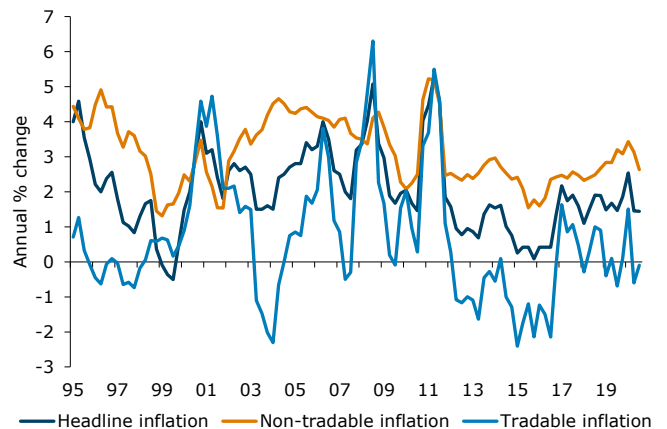
	% qtr	% ann
Headline CPI	0.7%	1.4%
Tradable	0.6%	-0.1%
Non-tradable	0.6%	2.6%

- Compared to our forecasts, the weaker print reflects weaker-than-expected inflation in transport (0.7% q/q), communications (-2.5% q/q), recreation (0.3% q/q) and personal care prices (0.0% q/q).
- Weakness in some areas, like recreation, culture and personal care, is symptomatic of the impact that the current downturn is having on services industries and those related to tourism in particular; domestic accommodation prices remain especially weak.
- Other price moves were broadly as expected, with a lift in household contents, other durables and electronics following lockdown, though the lift in clothing and footwear after last quarter's plunge was smaller than expected.
- The prices of food, petrol and housing (and related prices like rates) rose broadly as expected, though rent and homeownership costs were a touch softer. These groups were the biggest contributors to quarterly inflation this quarter, contributing 0.6%pts combined.
- Core inflation measures drifted even lower. These are more difficult to interpret than usual, but the trend is nonetheless concerning. The weighted median measure fell 0.2%pts to 2.2% y/y. Trimmed mean measures fell across all levels of trim, with the 15% trim falling from 1.8% to 1.6% y/y – all trimmed mean measures are now sitting below the RBNZ's 2% target midpoint. The RBNZ's sectoral factor model is released at 3pm and will be less affected by CPI weights.

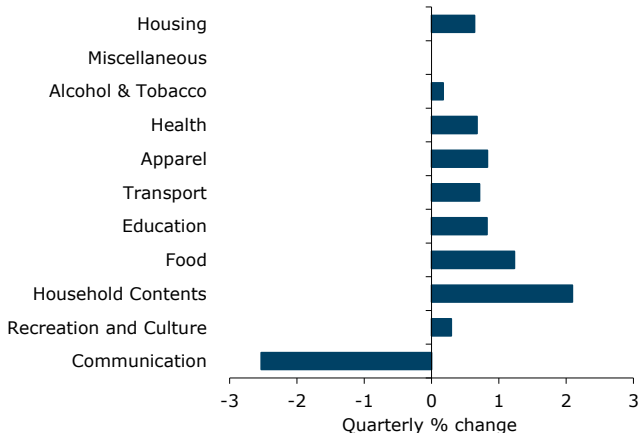
**Figure 1. Headline CPI inflation**



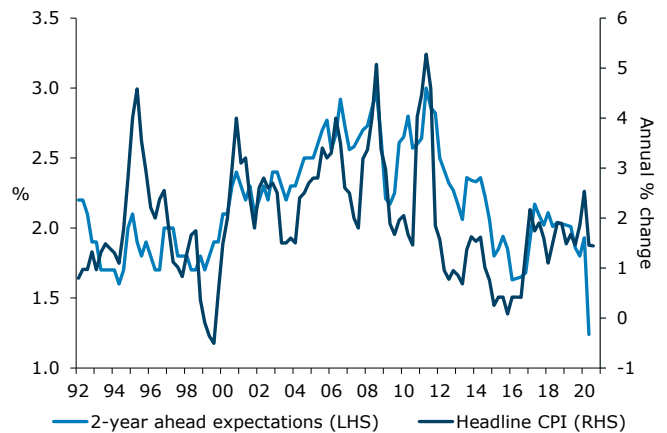
**Figure 2. CPI inflation components**



**Figure 3. CPI groups – September 2020 quarter**



**Figure 4. Inflation expectations & headline inflation**



Source: Statistics NZ, RBNZ, ANZ Research



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